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The Changing Fact of North America in the Global Economy

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I. History of North American Integration

A. Early Efforts

Economic, cultural and political ties between the nations of North America are not a new phenomenon. The United States and Canada have an extensive history of cooperation, having recognized the transborder aspects of water management, pollution control, immigration and other "domestic" policies for well over a century. Over 200 treaties are now in force between the U.S. and Canada governing boundaries, commerce, the environment, energy, immigration and other areas [See Tables 1 and 2].

Management of shared water resources provides a good example of successful early efforts at deep seated cooperation. The U.S.-Canada Boundary Water Treaty of 1909 gave official recognition to the need for bilateral management of boundary waters and established the principle that neither country should exploit the waters in a way that would damage the interests of the other. The treaty established the International Joint Commission, a binational group charged with overseeing water management, and later, broader areas of transborder environmental protection and conservation.

In the economic sphere, commercial ties between the U.S. and Canada were crucial to many New England and Canadian communities well into the 19th century, especially after the British adopted free trade and its North American colonies lost their imperial advantages. This actually led to demands by some Montreal merchants for annexation by the United States, but a more satisfactory arrangement was a free trade (in resources) agreement in 1854. Termination of the 1854 agreement during the U.S. Civil War helped to drive the movement for Canadian Confederation in 1867 and ultimately the Canadian National Strategy in 1879, which introduced high Canadian tariff walls.

In subsequent years, interest in bilateral free trade surfaced off and on. A tremendous upsurge in U.S. foreign direct investment (FDI) in the 1960's revived this interest in both countries, and found its most concrete expression in the 1965 Automotive Products Agreement between the U.S. and Canada. The Auto Pact provides for duty-free treatment of finished vehicles and parts between the two countries and helped set in motion a process which eventually led to a comprehensive free trade agreement (FTA) more than two decades later. The Auto Pact both responded to, and stimulated, rationalization in the North American automotive industry.

On yet another level, Alberta and Montana, Quebec and the New England states, British Columbia and Washington, Ontario and the Great Lakes states, and New York and Quebec have all enjoyed close relations. Their functional agreements to cooperate in such areas as energy, trade, the environment and education have enriched our binational cooperative efforts. These relationships were extensive enough to cause the U.S. State Department to conduct a 1976 study which found that state/provincial interaction was "pervasive in scope, extending to all functional areas of governmental activities."

Like Canada, the history of cooperation on the U.S.-Mexican side is focused along the border. A 1884 U.S.-Mexican Treaty led to what is now called the International Boundary and Water Commission, which has jurisdiction over all questions arising from changes or alterations in the Colorado, Tijuana and Rio Grande Rivers. Formal bilateral economic cooperation accelerated much later, especially in conjunction with Mexico's unilateral economic reforms and its accession to the GATT. Early steps on the road to regional free trade included a tariff reduction agreement reached in 1979, a subsidies code in 1985, and a Trade and Investment Facilitation Agreement in 1987.

B. U.S.-Canada Free Trade Agreement

A distinguishing feature of U.S.-Canada relations is the significant commercial interaction that predates the formation of our national boundaries. Business-driven integration, augmented by this rich history of government cooperation, made our two countries ripe for a free trade agreement.

As we entered the 1980's, the United States and Canada had the largest bilateral trade relationship in the world, with $80 billion in two-way trade, and a combined $55 billion in foreign direct investment in both economies. Since 1879, a key motivation for bilateral foreign direct investment had been for U.S. companies to get behind Canada's high tariff walls in order to service the Canadian market. In the 1980's, however, the magnitude and nature of economic integration began to accelerate rapidly with a sharp upswing in international direct investment and inter-firm collaboration. From 1980 to 1989, the year of implementation of the U.S.-Canada Free Trade Agreement (CFTA), the stock of U.S. direct investment in Canada grew from $45 billion to $64 billion, while Canadian direct investment in the U.S. grew from $10 billion to $30 billion.

Growing investment was a catalyst to the trade boom. As our firms expanded and organized their operations more broadly, exports to each other's markets more than doubled in both directions, a rate substantially in excess of our 50 percent export growth to the rest of the world.

Of course, the enormous business pressures leading up to integration did not occur in a political vacuum. In 1984, Prime Minister Mulroney approached President Reagan with his interest in developing a free trade framework to counter what Canadians perceived to be a growing protectionist color to U.S. trade policies and lagging Canadian competitiveness. President Reagan, who had espoused the idea of a North American trade pact in his 1980 campaign, responded positively. The next five years were the subject of progressively widening negotiations.

Just as we saw in the run-up to EC 1992, the prospect of change surely influenced business decisions and stimulated some of this pre-CFTA business activity. Nonetheless, given the long history and extent of our commercial relations, it appears that governments were largely catching up with what firms were already doing.

C. NAFTA: Turning South

In contrast, on the U.S.-Mexico side, the dominant role of government is indisputable. When the NAFTA negotiations were launched in 1991, it was the unilateral economic reforms of Mexico that were the *sin qua non* for moving integration forward. Not only did Mexico's accession to the GATT open its economy to greater competition, but the entire Mexican economy was reshaped as the Mexican Government privatized entire business sectors. The economic resurgence that followed was the lubricant for a dramatic upswing in bilateral trade and investment.

Between 1986 and 1993, U.S. exports to Mexico more than tripled, with Mexico surpassing Japan as the second largest market for U.S. industrial exports. Similarly, U.S. imports from Mexico doubled, with much of this growth in semi-manufactures and components that complement U.S. production. Two-way trade rose from $30 billion to $82 billion in just seven years. At the same time, U.S. portfolio investment soared, based on attractive real dollar returns on peso-denominated instruments and heavy foreign interest in Mexican stocks, reaching a cumulative level of an estimated $45 billion in 1993. With NAFTA's imminent approach, U.S. foreign direct investment in Mexico increased $5 billion in just the last three years preceding the treaty.

By the time we actually signed NAFTA, business underpinnings had been strengthened significantly between the United States and Mexico. Clearly, it was this coupling of market and policy developments that gave momentum and credibility to NAFTA.

The process had come full circle. Unilateral reforms by the Mexican Government inspired a broad coalition of business and government interests to "lock in" these gains. The coalition consisted of the Mexican private sector which was enjoying strong growth for the first time in a decade; the U.S. and Canadian private sectors which wanted continued trade and investment access to the Mexican market; the Government of Mexico, which sought to give permanence to this new direction; the U.S. Government which saw the opportunity for a wide range of benefits in a new relationship with Mexico; and the Government of Canada, which wanted to ensure that Canada would not be disadvantaged by any new expansion of regional trade.

II. North American Integration — A Current Snapshot

Before looking ahead to where we are going, it is important to understand where we are. Let me begin with the extent of economic integration that now exists in North America. At the outset, I would suggest that the phenomenon of "North American economic integration" is of a qualitatively different nature than merely denser networks of trade — it is based on complex, cross-border corporate production, distribution and sourcing networks and on increasingly tight linkages in infrastructure. This makes it difficult to describe the relationship in traditional international trade/foreign investment terms. In cases like the automobile industry, for example, talking about "trade" between the U.S. and Canada makes about as much sense as talking about "trade" between Michigan and Ohio. Nonetheless, there is value in putting some parameters around the North American trade and investment relationship, even if such data suggest artificial boundaries in some instances.

A. Investment

Foreign direct investment among the three NAFTA partners has doubled in the last decade, reaching just over $120 billion in 1992 [See Table 3]. We are principal investors in each other's markets.

The United States is the largest foreign investor in Canada and Mexico, contributing roughly 65 percent of total foreign direct investment (FDI) in both Canada and Mexico [See Figure 1]. The share of total U.S. FDI going to our North American neighbors (16 percent) is substantially larger than one might expect based on Canada's and Mexico's share of world GDP (4 percent). Looked at from the point of view of our neighbors, the United States is the most popular destination for Canadian and Mexican FDI; Canada, in particular, is the 4th largest foreign direct investor in the United States.

Canada and Mexico's past import substitution policies have been a major incentive to U.S. foreign investment in these markets; more recently, a larger share of U.S. FDI appears to have been devoted to developing continental and global production strategies. Fifty-two percent of U.S. FDI in North America is in manufacturing; this compares to 35 percent for our FDI in the rest of the world [See Figure 2]. Canadian and Mexican FDI in the U.S. shows a similar concentration in manufacturing, 45 percent of the total.

Portfolio investment within North America has been growing even faster than foreign direct investment. After doubling during the 1980's, portfolio investment among the three countries climbed from $142 billion to $175 billion in just three years (1989-1992). Preliminary estimates suggest that U.S. portfolio investment in Mexico rose further from $22 billion in 1992 to an estimated $45 billion in 1993. A major goal of the Salinas Administration was to attract more of this capital in the form of direct investment. The new government of President Zedillo is equally committed to maintaining an economic climate conducive to private investment.

B. Trade

Even more remarkable than our investment performance has been the explosion of trade within North America. Between 1980 and 1993, intra-North American trade increased by 170 percent, 50 percent faster than our trade with the rest of world. This is a truly remarkable development if you consider the other dramatic structural changes over this period — rapidly rising U.S. automobile imports from Japan, the emergence of the Asian tigers as important global suppliers and consumers, etc. [See Figure 3].

North American integration is even more pronounced if we focus on exports, with intra-North American exports growing twice as fast as North American exports to the rest of the world. As a result, today intra-North American exports stand at almost $300 billion; $4.60 out of every $10 that North America exports — almost half our total exports to the world — are sold to each other [See Figure 4]. Thus, North American trade integration is approaching European levels, where other EC markets account for 60 percent of total EC exports.

The dynamism that is occurring here in North America has given us a tremendous boost. Just as international trade has been a driver of global economic growth, so too has intra-North American trade been a driver of North American growth. Since 1980, intra-North American trade has grown twice as fast as North American domestic investment and almost 30 percent faster than North American GDP [See Figure 5]. Growing trade integration in North America has been a major job creator and a source of economic energy.

Despite our growing economic importance to each other, as a region we are not looking inward; in fact, we continue to exert considerable influence in global and other regional economic groups. North America accounts for 18 percent of total world trade and almost 45 percent of APEC's trade. The latter is particularly interesting, given the tendency of some observers to treat NAFTA and APEC as competing blocs.

As these figures demonstrate, there can be no doubt that North American integration was already substantial on the eve of launching NAFTA. Sidney Weintraub, a noted authority on U.S.-Mexican trade with the Center for Strategic and International Studies, perhaps characterized NAFTA best as "a way of formalizing *de facto* integration."

C. Characteristics of the North American Market

Nonetheless, expanding and adapting the CFTA to incorporate Mexico was a major event. Debate in the U.S. focused on Mexico's lower income, lower wages and weaker environmental record; in contrast, Canada's high-tech and natural resource-based economy was perceived as a natural partner to the United States.

In truth, the similarities between Mexico and Canada, as seen from the U.S. perspective, are as compelling as the differences. The fact is, North American trade shares a number of features in common. These features not only emphasize our extensive economic linkages, but they help explain how regional integration can make us more competitive.

1. Movement Away from Substitution Policies

Prior to formal integration, both Mexico and Canada retained significant tariff barriers — each about 10 percent compared to 4 percent for the United States. This tariff structure formed a considerable barrier to market entry and was symbolic of their general approach to trade — tariffs and nontariff barriers (NTBs) across a wide range of goods promoted domestic production for a limited, sheltered market. The CFTA, and now NAFTA, represent an important policy shift: an embrace of competition to improve the national capability to compete in global markets.

2. Preference for One Another's Products/Markets

Unquestionably, we are best markets for each other. Mexico and Canada each source 70 percent of their imports from the United States, roughly 5 times our share of world exports. Further, the United States is their largest market, responsible for the preponderance of their foreign sales (76 percent for Canada and 78 percent for Mexico). Thus, we get the greatest return in future sales when our imports come from one another. As Canadian and Mexican sales to the U.S. generate growth in their economies, they in turn are more likely to increase their purchases of U.S. products.

3. Extensive Coproduction within North America

The United States is engaged in extensive production-sharing arrangements with Mexico and Canada that are characterized by their high proclivity to use U.S. inputs.

Many firms engage in production-sharing with foreign companies or affiliates. Japan, Mexico, Germany and Canada account for three-quarters of all coproduced imports that return to the United States for final assembly or sale.[1] The use of U.S. inputs by these countries varies widely, however. Mexico uses more U.S. inputs than the others by far (52 per-

1. International Trade Commission, *Production Sharing: U.S. Imports Under Harmonized System Provisions 9802.00.60 and 9802.00.80, 1989-1992*, Feb. 1994 (USITC Publication 2729). Based on data for a program the United States set up specifically to encourage the use of U.S. inputs in production-sharing abroad by offering duty-free treatment on the U.S. content if the coproduced product enters the United States.

cent), followed by Canada (33 percent); in contrast, Japan and Germany have less than 3 percent U.S. content in their coproduction products. Looked at another way, half the value of coproduced imports from our NAFTA partners originates in the United States, compared to an average of only 15 percent for goods coproduced outside North America [See Figure 6].

Consequently, when U.S. firms decide global competition requires a global production strategy, the United States retains a much greater presence in the production process when the arrangement involves a North American partner. Shorter supply lines, just in time delivery, and ease of return are just a few reasons why proximity really does make a difference.

4. High Degree of Intra-Industry Trade

The bulk of North American trade takes place in just a handful of products. Fully 60 percent of all intra-North American trade occurs in just 9 industries. Typically, the same industries are national leaders in both exports and imports, with the most notable exception being crude petroleum (which figures importantly in U.S. imports from its NAFTA partners but not in its sales to them) [See Table 4].

What we are seeing is that regionalization tends to accentuate broad similarities in national production. That helps explain why, despite the significant differences in the Canadian and Mexican economies, the top three U.S. exports are the same to each; moreover, these same products figure importantly in our imports from them.

Regionalization, like globalization, appears to intensify local specialization *within industries.* Thus, rather than resulting in a discrete allocation of industries among countries at the regional level, with one country "winning" one industry (like autos) while another takes over a different industry (say, steel), rationalization at the regional level seems to distribute business within key industries across the three economies.

5. High Degree of Intra-Firm Trade

Not surprisingly, much of that intra-industry specialization is actually occurring *within companies.* We know that almost half of U.S. trade with our North American partners consists of transactions between firms with some common ownership. Much of this trade is in the commodities listed in Table 4.

Moreover, more of U.S. trade within North America takes place between related parties (47 percent) than is true for the rest of the world (36 percent) [See Table 5]. No other country exceeds Canada and Mexico in the importance of related party sales in U.S. export transactions, which stands at 45 percent for Canada and 39 percent for Mexico. On the import side, the most distinguishing feature is the high proportion of U.S. imports from Mexico that are between related parties (only imports from Japan are higher). In large part, this reflects the extensive assembly operations along our border; however, the sharp contrast in related party exports to Mexico (39 percent) and related party imports from Mexico (64 percent) suggests that more of U.S. exports to Mexico are going to independent purchasers than is commonly perceived.

Sales through exports are only one means of doing business in foreign markets. U.S. firms actually sell just as much to Mexico and Canada through the sales of their affiliates located in these markets. In 1991 (latest year available), U.S. affiliate companies sold over $128 billion of goods and services in Canada and over $17 billion in Mexico. While U.S. affiliate sales are somewhat more important than exports in selling to Canada, U.S. exports to Mexico are twice as large as the sales of U.S. affiliates located there.

Increasing intra-firm trade generates its own form of competition, with large corporations playing units off against one another. As the branch plant system (that is to say, affiliate firms set up in another country primarily to serve the foreign market) is increasingly replaced by the integration of these firms on a continental basis, a major focus of competition is within firms, among operating units competing for production mandates. This trend is reinforced by new technologies that heighten productivity. Thus, for example, as the number of GM assembly operations decreases, the most intense competition each unit faces is with the other units in the GM organization.

III. Economic Payoff of Integration

Integration in North America produces broad based economic benefits that accrue to the entire region.

A. Experience Under the CFTA

Although it is far too early to detect definitive trends in our trade with Mexico as a result of NAFTA, the CFTA provides one gauge of the Agreement's *potential* impact.

The first five years of free trade between the United States and Canada have witnessed a progressive rise in trade volume despite the fact that relatively slow domestic economic growth in both countries should have suppressed demand. Total bilateral trade in goods and services grew by $68 billion, from $169 billion in 1988 (just prior to the CFTA) to $237 billion in 1993.

Critics of the CFTA in Canada have blamed Canada's recession and weak, economic performance since 1989 on free trade. In fact, studies published by both the Bank of Montreal and the C.D. Howe Institute argue that free trade helped to mitigate the effects of the economic downturn. During the period coincident with the CFTA, what little growth Canada recorded was almost entirely attributable to strong export performance. Moreover, the strongest export growth was to the United States, whose demand for Canadian products grew almost one-third faster than Canada's non-North American trading partners.

The C.D. Howe Institute, which also analyzed the product composition of Canada's export growth, found that growth was strongest in sectors liberalized by the CFTA.[2] For these products, Canadian merchandise exports increased 33 percent to the United States, compared with only a 2 percent increase to the rest of the world.

For the U.S. part, U.S. exports to Canada during this period grew faster than our exports outside of North America, and our already high share of the Canadian market increased. A study by the U.S. Department of Commerce suggests that many U.S. producers became newly competitive in the Canadian market as the result of tariff removal under the CFTA.[3] Important gains were realized in key product categories; in fact, 46 out of 98 product categories with significant tariff decreases have grown 100 percent or more since the CFTA became effective. Moreover, several traditional import sensitive sectors in the United States, such as apparel and furniture products, saw their exports rise rapidly as the CFTA lowered Canada's substantial tariffs on these goods.

2. Daniel Schwanen, "A Growing Success: Canada's Performance Under Free Trade," C.D. Howe Institute Commentary No. 52 (September 1993).
3. Jeff Hawkins, "Canada-U.S. Free Trade Agreement: An Interim Assessment," *Business America*, U.S. Dept. of Comm., (April 20, 1992).

The CFTA also spurred cross-border investment flows. As has been the case with EC 1992 and NAFTA, such investment often begins prior to the formal event as firms anticipate the effects of an agreement. Thus, between 1987 and 1992, bilateral direct investment in each other's economies grew by $24 billion, from $83 billion to $107 billion in 1992. While these investment flows were split about evenly in each direction, Canadian firms realized a 58 percent increase in their direct investment in the U.S. while U.S. firms increased their already substantial FDI in Canada by 18 percent.

Likewise, net foreign investment flows in the CFTA trade area swelled due to the increased attractiveness of both markets. In fact, in 1990, for the first time in 16 years, Canada experienced a net inflow of foreign direct investment, which continued in 1991 and 1992. The Royal Bank of Canada suggested that this was "broadly consistent with the view that the free trade agreement between Canada and the United States has enhanced Canada's attractiveness for foreign investment."[4]

Free bilateral trade under the CFTA has stimulated job creation in the United States and Canada. In contrast, there have been few major dislocations, as the process of transition and adjustment has been phased in under the Agreement.

Many of the sectors experiencing growth and job creation through increased North American integration are higher paying, higher value-added sectors in both countries. For example, an estimated 200,000 new American jobs have been created and are dependent upon U.S. exports to Canada, increasing from 1.3 million in 1988 to 1.5 million in 1993. Much of this export growth and net job creation has occurred in high-technology industries such as computers, communications, electronics, software, plastics, and scientific instrumentation, in addition to the business services supporting these sectors.

Similarly, the C.D. Howe Institute found that in Canada, significant export-led growth and expansion is occurring in such high wage sectors as business services, high-technology industries, and natural resources. The study also concludes that the CFTA is resulting in greater specialization of the economy, moving Canada into areas of higher productivity and income.

B. Projections Under NAFTA

NAFTA is probably the most thoroughly studied trade agreement in history. In his speech signing the side agreements to NAFTA, President Clinton observed that nineteen out of twenty serious studies showed that NAFTA was good for the U.S. economy and U.S. labor.

Nonetheless, economists agree that the greatest effect of NAFTA will be on Mexico. This is quite natural as Mexico has the smallest economy of the three nations and the highest barriers. Further, as noted above, the CFTA already offered the U.S. and Canada substantial benefits from greater integration.

A study done by the Congressional Budget Office (CBO) for the U.S. Congress just before the vote on NAFTA explains how the regional synergies work.[5] A good starting point is the NAFTA-induced reduction of the risk premium that Mexico must pay to attract international capital. The CBO estimates that Mexico's risk premium will fall an estimated 10

4. Royal Bank of Canada, "Free Trade Agreement: Two-Year Retrospective", *Econoscope*, (Feb. 1991).

5. Congressional Budget Office, *A Budgetary and Economic Analysis of the North American Free Trade Agreement*, (July 1993).

percentage points over a three year period following implementation of the NAFTA (recent political developments may delay this drop, but I believe the fundamentals that would cause it are still present.) Less expensive capital will enable Mexico to finance a current account deficit that is expected to grow as a percentage of its GDP, as Mexico imports more plant and equipment to fuel the growth of its economy. Coupled with improvements in productivity, the CBO judges that Mexico is likely to achieve annual average output growth of 6 percent over the next decade. (All CBO scenarios show higher Mexican GDP growth as a result of NAFTA and economic reform).

Simply put, higher Mexican economic growth triggers faster U.S. (and to a lesser extent, Canadian) economic growth as well. Mexico's GDP is only about 5 percent of that of the United States. As such, the NAFTA is estimated by the CBO to add only about one-quarter of a percentage point to U.S. GDP. However, the U.S. GDP in 1993 was $6.4 trillion; one quarter of a percent of that is $16 billion — a not inconsequential amount. The increase in U.S. national income will come not only from increases in U.S. exports to Mexico, but also from repatriated profits and dividends from investments in Mexico.

All in all, the Clinton Administration anticipates NAFTA will have generated 200,000 more export-related jobs by January 1995, pushing U.S. employment related to exports to Mexico toward the 1 million mark. Contrary to the fears of U.S. labor, we expect NAFTA to increase the demand for U.S. unionized workers. Our experience since 1987 shows that Mexican demand for U.S. goods is most intense — and Mexico is least competitive — in precisely those high wage, capital intensive, heavy manufacturing industries which are heavily unionized.[6]

NAFTA is already working. U.S. trade data for the first nine months of 1994 show NAFTA trade accelerating, particularly in regard to U.S.-Mexico trade where NAFTA's changes are most significant. Despite some slowness in Mexico's economic recovery, U.S. exports so far this year are up 21.7 percent over the same period last year; in contrast, in 1993 slow Mexican growth held U.S. export advances to less than 3 percent. On the flip side, while one would expect Mexican sales to the U.S. to respond to our economic recovery, they are up a robust 23 percent — twice as fast as our import growth from the rest of the world. (Both export and import growth with Canada are up a respectable 8 percent.)

Coupled with other trade developments, the results add up to an impressive picture for NAFTA in the United States: so far in 1994, Mexico and Canada account for a whooping 88 percent of U.S. export growth and only 28 percent of our import growth.

Reinforcing this positive trade picture, we have not seen any early signs that NAFTA might lead to substantial job dislocation in the United States. Through November 1994, the Department of Labor has certified 12,015 workers (based on 114 positive determinations) as eligible for NAFTA's transitional trade adjustment assistance. This number is far less than that warned of by NAFTA's critics, and suggests that we are in a good position to provide for those workers who bear the adjustment of NAFTA's contribution towards developing a more competitive U.S. economy. It is notable that in an effort to ensure that this assistance is readily accessible to those who need it, the trade adjustment program requires only that workers demonstrate an increase in imports from or a production shift to Mexico or Canada, not a causal link to NAFTA.

6. "NAFTA and the Employment of Union Workers in Manufacturing," Council of Economic Advisors and the U.S. Treasury, (Nov. 8, 1993). (Nor have the expanding exports of heavily unionized sectors been offset by import gains).

IV. New Structures: Private Sector Response to NAFTA

North American businesses are operating in new ways in response to NAFTA's changes. Because NAFTA creates more options for serving the North American market, firms have greater flexibility to determine how best to take advantage of the new opportunities.

Corporate strategies to respond to the integration of the North American economy are comprehensive. Some firms are responding through increased production and new investments in their home markets, while for others, inter-firm agreements and strategic alliances at the transnational level will generate a new regional dynamism. In either event, firms are rationalizing and restructuring to take advantage of NAFTA.

Business development strategies for addressing a unified North American market must be responsive to specific industry and company needs. The choice will vary from company to company; no one approach will work for all.

A. Expanding Home Base

Companies are now freer than before to choose their preferred method of serving an expanding customer base. For instance, with the elimination of tariff walls as a basis for production location decisions, some firms can service their North American customers most economically by exporting from their home base. Many companies are meeting increased demand by retaining or expanding their national production capabilities or simply redirecting resources to exploit more fully existing capacity.

This is the case for Health-Mor Inc., which decided to keep production in Cleveland, Ohio, rather than to move to Mexico after NAFTA removed the $50 Mexican tariff on its $1,200 vacuum cleaners. Panamax, a small California company that designs and manufactures surge protectors for high-tech electronic equipment, added an additional shift of production workers in order to meet NAFTA-generated sales. Similarly strapped for capacity, Ace Hardware, based in Oakbrook, Illinois, plans to open a $26 million paint manufacturing facility in Texas as a result of NAFTA. Regional export sales spurred by NAFTA have led to job increases and higher profits for these firms.

Even for industries that already have a relatively high degree of North American integration, the removal of many non-tariff barriers is allowing them to rethink their approach to the North American market.

The auto industry is a good example. Prior to NAFTA, the Mexican Auto Decree dictated the terms of production and sale in Mexico. Among the more onerous requirements was a "trade-balancing regulation" that required auto manufacturers to produce and export from Mexico $2 worth of vehicles for every $1 worth of imports. NAFTA phases out this and other restrictions over ten years.

NAFTA makes substantial vehicle exports to Mexico from the U.S. a serious possibility for the first time. As a result, this year Chrysler Corp. plans to export to Mexico 2,500 Dodge Intrepids built in Newark, New Jersey, and 3,000 Jeep Cherokees produced in Toledo, Ohio. General Motors has announced its plans to export 15,000 cars and trucks to Mexico in 1994, up from only 1,700 in 1993. To satisfy increased demand for their cars in Mexico, Ford is expanding production of the Escort subcompact at its Wayne, Michigan facility. All in all, the Big Three expect to export 55,000 cars and trucks in 1994, compared to only 5,000 vehicles in all of 1993.

B. Organizational Focus

For many large firms, the initial response to NAFTA is to create some type of North American organization or business unit. In fact, the Council of the Americas confirmed this trend in a survey last year. We are finding this kind of North American reorganization to be true even of companies that had not previously been in all three markets — such as Heinz of Pittsburgh, Pa., which has substantial sales to Canada but none yet to Mexico. Prompted by NAFTA, Heinz formed a North American unit to examine the possibilities for achieving greater economies of scale.

Warner-Lambert decided to centralize control of its Canadian, Mexican and U.S. operations in 1992, in anticipation of NAFTA. Under the new entity, Park Davis North American, relationships between the three divisions have been reconfigured, allowing the company to centralize operations when necessary as well as respond locally when desirable to do so. The result streamlines production and minimizes inefficiencies.

These types of actions allow firms to assume a strategic North American outlook and serve a unified, North American customer base rather than three distinct markets.

C. Rationalizing Production Lines

Increasingly, trade around the world is being restructured by the investment plans and collaboration agreements between firms that are organizing their activities globally. NAFTA will provide an additional impetus to this phenomenon in North America. Thus, while NAFTA at its core is a trade agreement, an important element of this is the new economic infrastructure NAFTA provides for corporate investment.

As North American companies become free to redeploy resources between the three countries, many larger firms with production capacity in one or more NAFTA countries are finding new and better ways to achieve economies of scale and serve a unified North American market more efficiently.

Many of these firms had built up dual systems of production in more than one country that became redundant once tariff impediments were removed. The need to better utilize excess capacity inevitably leads to the rationalization of production lines.

For instance, shortly after implementation of the CFTA, Whirlpool ceased washer production at its Inglis, Ontario plant, and instead, begin importing washers with more advanced technology from its plant in Clyde, Ohio. Shutdown of the plant was part of a North America-wide reorganization, which also provided for the movement of some dryer production to a newer plant in Inglis.

D. Strategic Corporate Alliances

Many U.S. companies are establishing strategic alliances with their Mexican and Canadian counterparts as a way to gain a stronger competitive foothold in a unified North American market. The nature of these alliances range from targeted joint ventures to mergers and acquisitions, depending upon the specific structural needs and business imperatives of the industry.

Access and control over distribution and sales channels is a crucial factor in successful marketing of *food and beverage* products. Pillsbury expanded its distribution and sales capacity in Mexico by purchasing a 49 percent stake in a joint venture with Pacific Star de Occidente to form a new company, Pacific Star. Increasing Mexican consumer demand, and a strong preference for U.S. food products, led Pillsbury to seek a way of improving the market position of its leading brands.

Similarly, Miller Brewing Company acquired a 20 percent equity share in Molson Breweries of Canada, as well as U.S. distribution rights for all Molson products. The purchase gives Miller better access to the Canadian distribution system, a financial stake in a competitive product, and control over distribution of that product in Miller's home market.

In the *financial* industry, Western Union and Elecktra Mexico are cooperating to market their products and services in a way that capitalizes on existing branch networks and name recognition without draining resources through outright acquisitions. Western Union entered into a cooperative venture with Elecktra Mexico that provides money transfer services from the United States to Mexico; it gives Western Union direct, immediate access to distribution channels for its services without costly establishment of new facilities.

In the area of *other services*, CN railways announced a marketing alliance with six U.S. railways in order to position itself for a greater share of the transborder freight traffic. As part of the venture, CN North America is spending $155 million to build a 1.8 km tunnel under the St. Claire river between Ontario and Michigan. A partnership with APL Land Transport is providing the first intermodal container service linking the U.S., Mexican and Canadian markets.

Some acquisitions provide supporting services that will facilitate the firm's principal sales activity. For example, the Chubb Insurance Group's purchase of a 30 percent interest in Seguros Equitativa and its affiliate, Central de Fianzas, gives Chubb control over the insurance, surety and bonding portions of its Mexican business operations.

Other mergers and acquisitions provide for market access. Following the Government of Mexico's privatization of the national telephone company, a consortium led by Southwestern Bell and including France Telecom and a Mexican partner Grupo Carso, successfully bid for a 20 percent equity in the new company, TELMEX. The purchase grants the new owners a six-year monopoly concession for basic *telecommunications* services lasting until August, 1996.

Technology and infrastructure needs are a powerful mix in high-tech firms. AT&T forged a joint business alliance with Unitel Communications, a major Canadian telecommunications carrier that will enable both companies to combine their national networks and offer a wider range of services. Unitel will use AT&T's proprietary network software and equipment in return for a 20 percent equity share.

Similarly, GTE recently announced expansion of its air-to-ground telephone network in Mexico and construction of a digital network in Canada, which means airline passengers will now be able to enjoy the convenience of placing phone calls while flying among the business centers of all three NAFTA countries. GTE formed a joint venture company with Telmex, Mexico's telephone monopoly, that will construct and operate a network of telecommunications stations to service this network throughout Mexico. GTE is upgrading its ground network in Canada as part of an already established relationship with Canada's Skytel Communications Corp.

A more exhaustive list of mergers, acquisitions and marketing alliances can be found in an Annex located at the end of this article. They all underscore the creativity and rapidity with which business can seek new partners to improve production and marketing in an expanded regional market.

V. New Structures: Regional Shifts and Cooperation

The dynamism of NAFTA is not limited to how business structures itself, but also extends to how change will effect the economic geography of North America. Trade flows will not move or grow evenly across borders. Rather, the flow of goods, services, capital and people will strengthen between the areas of each country that share common interests and are linked by transportation networks.

A. The Emergence of Trade Corridors

This creates the possibility under NAFTA for dynamic "trade corridors" to emerge that link all three countries, bringing enhanced economic benefits to communities and businesses located along these routes. Communities along these north-south corridors may have many more common interests with their counterparts in Canada and Mexico than they do with other U.S. regions, even those that are contiguous.

We have already seen this phenomenon as a result of the U.S.-Canadian Free Trade Agreement. An example is the existence of cross-border entities such as the "Pacific Northwest Economic Region" (PNWER), which comprises three Canadian provinces and five U.S. states joined together to promote the economic development of the region. Similar cross-border arrangements exist between U.S. states and Canadian provinces to share hydroelectric energy, coordinate environmental policy in areas like acid rain reduction, jointly plan transportation systems and promote regional tourism.

The addition of Mexico to the U.S.-Canadian free trade agreement creates even more interesting possibilities. The major trade links between the United States and Canada are in the Niagara (Buffalo-Hamilton) and Michigan (Detroit-Windsor) frontiers. Between the U.S. and Mexico, the largest share of commercial freight passes through Laredo, Texas and Nuevo Laredo, Mexico. These major gateways are connected through major trade routes originating in Montreal and Toronto, passing through the Eastern U.S., southeast Michigan and the industrial Midwest, and ending in the industrial heart of Mexico, in Monterrey, just 150 miles to the south of Laredo. The major border crossings in Laredo, Buffalo and Detroit act as "funnels" focusing trade routes that pass through the U.S. in what are currently rather diffuse patterns. The development and improvement of these routes is critical to an integrated North American market.

This major Eastern Americas pathway is not the only emerging North American trade corridor. Separate land transportation routes link Canada and Mexico through the Pacific Northwest/California, the Rocky Mountains, and Upper Plains. Current predictions of future trade flows indicate that the eastern corridor volume between the U.S. and Canada will increase at an annual rate of 5 to 7 percent through 1997. Western route traffic between the U.S. and Canada is expected to increase by 16 to 24 percent over the next ten years.

At the major U.S.-Mexico gateways along the North American trade corridors, expectations are that commercial trade volume will grow even more dramatically. A study by the U.S. Department of Transportation predicts that trade through Laredo will increase by 120 percent by the year 2000, through El Paso and the Rocky Mountain trade corridor by 110 percent, and through the California trade corridor gateway in San Diego by over 200 percent.[7]

7. *Assessment of Border Crossings and Transportation Corridors for North American Trade: Report to Congress*, Federal Highway Administration, U.S. Dept. of Trans., (Sept. 30, 1993).

The rail and truck land transportation corridors running through North America comprise between 80 and 90 percent of trade between the U.S., Canada and Mexico. This is not the whole picture, though. Significant amounts of intra-North American trade pass through ports and the intercoastal waterway systems. The Great Lakes and St. Lawrence Seaway system are critical transportation links between the U.S. and Canada, connecting the intercoastal waterway systems of the two countries. Freight can pass from Canada through the St. Lawrence Seaway, directly into the Mississippi River basin and the U.S. intercoastal waterway system.

The U.S. and Mexico do not currently have a such an inland waterway link, but as a direct result of NAFTA, the governor of the Mexican state of Tamaulipas has developed a comprehensive plan that could be completed by the end of this century to link Mexico's intercoastal system to the southern U.S. Gulf Intercoastal waterway system through Matamoros, Mexico and Brownsville, Texas.

U.S. and Mexican seaports are also integral parts of the North American trade corridor network. High traffic Gulf Coast ports like Houston and New Orleans have been actively forging links with the Eastern Mexican Port of Veracruz (the busiest port in Mexico). This port-to-port route provides a much more direct route to the huge Mexico City market than the land routes through Texas. Even before NAFTA, almost $5 billion in trade passed through this route.

These evolving trade routes will have enormous implications not only for the economies of these regions and the geography of North America, but also for popular support for NAFTA. Communities that find themselves along these evolving trinational trade corridors will identify more with the prospects for an increasingly integrated North American market. In fact, rather than passively waiting to see what shape NAFTA takes, many communities and state and local governments are competing for the opportunities.

In an interesting East-West twist, the Port of Miami has been actively promoting a trade link with the Yucatan ports of Merida and Progreso, realizing that they are in fact closer to these important ports than either Houston or New Orleans. Port of Miami officials see this as a long-range strategy that will ultimately set up triangular trade between Mexico, South Florida and Miami's major markets in the Caribbean and South America — our future hemispheric trade corridor, if you will. Such a development should help engender the support of the large Florida Hispanic population that stayed relatively passive during the NAFTA debate, in part out of concern that Mexico would divert trade from more established Latin routes.

Recognizing the importance of the links between U.S. and Mexican ports, the Government of Mexico is undertaking major modernization at the Veracruz and Merida seaports, along with those that form key links to the Western North American trade corridors such as Manzanillo and Lazaro Cardenas. Under this program they will invest over $1 billion in port improvements over the next five years.

In another example, the Governor of Kansas recently travelled to Mexico, specifically to build connections between her state and the governors and business communities of the southern end of the North American trade corridor passing through Kansas. An interstate business and government I-35 coalition has recently been formed, to build support for the recognition of the Interstate-35 highway connecting Laredo, San Antonio, Kansas City, Chicago and Detroit, and to seek additional federal funding. They have already made connections with their counterparts in Canada and Mexico along the same North-South trade corridor (Toronto, Montreal, Nuevo Laredo and Monterrey). A similar coalition has sprung up along the Rocky Mountain corridor.

We can expect to see more of this type of active exchange based on common economic interests between *regions* of North America to accelerate during the coming years. Just as the development of the U.S. interstate highway system had a profound effect on linking our communities and creating a national cohesiveness, so too will these new corridors create avenues of regional cohesiveness.

VI. New Institutions: Government Response to NAFTA

NAFTA's changes to our regional trade and investment regime require new approaches and new government institutions to respond effectively to the emerging commercial landscape.

The broad scope of NAFTA makes this particularly true. NAFTA is the first trade agreement to address comprehensively the "new" issues of investment, services, and intellectual property rights. Moreover, NAFTA broke new ground in its Supplemental Agreements by considering the interaction between trade and the environment, and trade and labor. New programs to address infrastructure deficiencies along the U.S.-Mexico border also were created to take account of the economic impact of trade on the environment.

Integration inevitably requires rules of the game to ensure that all parties have a full opportunity to realize the potential benefits. The economic incentives in a North American free trade area are a powerful motivator to create a system that works. The new institutions that follow represent the common mechanisms into which we were willing to channel our common aspirations.

A. Dispute Settlement

The significance of any trade agreement depends in large part on its ability to deal with differences over interpretation of the Agreement.

Like CFTA, NAFTA creates a Commission that meets regularly to review the implementation of the Agreement and to set out the work program, review trade relations among the members, and discuss problems that arise. Disputes that cannot be resolved through consultation may, at the request of a disputing Party, be subject to a panel review.

Regarding the CFTA, the most remarkable feature is how few disputes actually got to the panel stage. By setting up a process that demonstrated we were willing to live with a strong rule of law, we designed a system that was highly successful in accomplishing *dispute avoidance.*

However, NAFTA did offer an opportunity to improve upon a few features of the CFTA dispute settlement process.

To guard against conflict of interest, a concern that did arise under the CFTA, NAFTA provides for Parties to agree on the roster of panelists; for panelists to be chosen by "reverse selection" (each country appoints only panelists from the other); for panel majorities to alternate between the disputing parties. These refinements will go yet a step further to ensure that decisions don't have the appearance of being politicized.

We also improved the quality of the decision-making by bringing in more expertise. Scientific review boards may be set up to advise panels on environmental and health and safety issues; panelists dealing with financial services issues must be experts in that field; and antidumping and countervailing duty panels should be comprised of judges, rather than trade practitioners.

Finally, NAFTA includes several novel features to help minimize problems arising from differences in our legal systems. When disputes arise between a company and a government regarding NAFTA's investment protections, the Agreement provides for resolution through binding arbitration. Instilling more certainty in the business environment should give a boost to investment in North America. For private commercial disputes, NAFTA encourages the use of arbitration and other alternative dispute settlement mechanisms. We want NAFTA to generate jobs in our factories, not in our courtrooms.

B. NAFTA'S SOCIAL AGENDA

NAFTA is an important political breakthrough in recognizing the relation between trade, the environment, and worker rights. "Through its supplemental agreements, NAFTA creates two new trilateral commissions to provide for cooperation, public participation and dispute settlement on environmental and labor matters. How we manage these new institutions will largely determine whether freer trade advances together with progress in protecting the environment and workers.

These new institutions are in uncharted waters. They will have to deal with the sovereignty concerns of each country; moreover, they are going to have to balance providing a proper framework for business decisionmaking without interfering in the daily conduct of business, which would risk the gains of NAFTA. Whether we succeed or fail will have a profound effect on our progress towards hemispheric integration and on our post-Uruguay Round agenda in the new World Trade Organization (WTO).

In the environmental arena, the prospects for breaking new ground are best when market-led and policy-led initiatives converge. Here I think the increasing global attention of not only environmental non-governmental organizations (NGOs), but also customers, to the environmental aspects of production, packaging, and disposal have already prompted business to integrate environmental considerations into their corporate structures and business strategies. It is increasingly common to find multinationals whose policies are to implement "best practices" in their foreign operations worldwide.

The private sector also is working toward a more integrated approach to worldwide environmental policy. The International Standards Organization is developing environmental management standards similar to the companion ISO-9000 series on industrial product quality standards. Canada has been selected as the site of the Permanent Secretariat for the effort, and the U.S. will chair one of the six subcommittees under this effort (environmental performance review).

Labor policies, on the other hand, tend to differ more among countries, reflecting local culture and practice. Less progress in convergence has made it more difficult for institutions such as the International Labor Organization to reach agreement on appropriate international standards against which to measure compliance. In the labor supplemental agreement, we agreed for the first time on a set of principles that provide for basic worker protections in North America.

Of all the labor issues, wages are the most contentious. This was dealt with indirectly in NAFTA by former President Salinas' pledge to increase minimum wages in line with rising labor productivity — a challenge for any of us.

This issue should defuse somewhat as Mexican workers' wages rise under NAFTA. Since the Mexican economy started growing again in 1987, Mexican wages have risen 37 percent. Mexican economic growth, spurred by NAFTA, is absolutely necessary to continue these gains.

In the immediate future, NAFTA's spotlight will be on the rights of workers to unionize. The U.S. National Administrative Office, the first point of contact for complaints about labor practices in our NAFTA partners, recently accepted for review two U.S. union submissions regarding freedom of association and protection of the right to organize in Mexico. This will be the first test of how we collectively deal with sensitive, sovereign issues under the scrutiny of public view.

One thing we'll have to watch out for — that our conduct of this process does not interfere with the daily conduct of business. Obviously, decisions to hire and fire are made every day, and we need to be mindful that the obligations of the Agreement are on governments to enforce their laws, not on individual firms.

We also will have to take a careful look at the relation between labor issues and broader economic policies. For example, U.S. longshoreman have recently complained that Mexico's efforts to privatize its ports have the effect of union-busting. Privatization is a key element in Mexico's drive for modernization and development, and we will have to strike the right balance between our efficiency and labor goals.

The new "social" institutions of NAFTA offer both the ying and the yang — more cooperation, but also more contention. Their development will determine whether NAFTA makes North America a more or less attractive site for business and investors. Done with vision and sensitivity, they offer North America the opportunity to exert leadership on parallel initiatives in multilateral fora.

C. Border Infrastructure

The U.S.-Mexico border became an important symbol in the debate over NAFTA: would further North American integration lead to runaway development or would it provide the means to deal with the long festering problems of inadequate infrastructure? In the end, there was a general recognition that only economic growth would provide Mexico with the means to tackle its environmental and infrastructure problems.

In the meantime, we identified steps that governments could take to improve the lack of coordination and funding for critical environmental infrastructure projects that would benefit both sides of the border. Hence, the bilateral North American Development Bank (NADBank) and the Border Environment Cooperation Commission (BECC) were born. The BECC, in particular, will be a powerful force for coordinating environmental cleanup along the border — not only between our two countries, but between often competing local jurisdictions. After extensive public hearings, the BECC will assist states, local communities and the private sector in sitting, arranging financing and applying environmental standards for border infrastructure projects it certifies.

It is the financing issue that is most critical. The problem is, governments can only do so much. The U.S.-Council of the Mexico-U.S. Business Committee estimates U.S.-Mexico border needs over the next decade at $5.8 billion for water-related and municipal waste projects alone; some have estimated overall needs may be as high as $20 billion. (Table 6 illustrates the range of infrastructure projects on the drawing board.) Even with substantial monies from existing sources, including multilateral development banks like the World Bank, the "financing gap" is considerable.

The solution is to get the private sector more involved, both through greater resort to user fees and through creative project financing for the region's needs. That message came through loud and clear in an infrastructure conference co-hosted by Secretary Brown and the late Secretary Colosio in San Antonio in July 1993 that was attended by some 500 top financiers and project developers. It underlies the principal the NADBank is based on: the need to leverage limited government resources with private capital.

Recently, we are seeing some innovative developments. For example, some 320 maquiladoras in Ciudad Juarez have pledged to contribute 25 percent of the cost of three wastewater facilities in the region that would benefit both the companies and their community; the federal and local Mexican governments would contribute 35 percent, with the remaining share provided by a private investor. If the plan goes forward, the companies will recoup their share through discounts to future water-use fees.

Also, Mexican officials are re-thinking their traditional financing sources. Local government leaders in Tijuana want to establish their own tax assessment districts to help finance a $117 million infrastructure project to build highways and pay for urban renewal. This is a typical form of financing in the United States that up until now has been unheard of in Mexico. Tijuana will seek the state government's approval of the plan under a 1984 federal law that has never been used.

In a truly innovative move, the U.S. Eximbank and Banobras, a Mexican bank, have agreed to a joint program that will make financing available for U.S. waste water treatment facility exports to *Mexican cities*. While user fees will be collected to pay for the equipment, the two banks will serve as loan guarantors if municipal payments lag.

There is also activity on our side of the border. The Arizona legislature just sent a border-development bill to Governor Symington to establish a new state authority which will work with the NADBank to finance infrastructure projects along Arizona's border.

Finally, one of the biggest steps in helping Mexico address its financing needs may be the decision of the OECD to invite Mexico to be the first developing country to join the ranks of the industrial nations. That vote of confidence for Mexico's economic progress may boost Mexico's prospects for achieving access to capital markets at better terms.

VII. Clinton Administration Efforts to Make NAFTA Work

Successful implementation of the NAFTA by the Parties is key to demonstrating the success of the Administration's export-led economic growth policy and for maintaining broad public support for meeting global competition through open markets. Our efforts to extend trade integration in the Hemisphere, as well as much of our post-GATT trade agenda, will depend on how well we implement NAFTA.

From the U.S. standpoint, the implementation of NAFTA has several components.

First, we are *monitoring Mexican and Canadian compliance* with the Agreement. We keep close contact with our business community so that we know when problems arise. So far, implementation has proceeded relatively smoothly. The most common problems we are hearing about are administrative in nature, such as customs enforcement, and are to be expected when putting such a massive change in place. The U.S. Census Bureau is reporting that between one-third and one-half of U.S. trade with Mexico and Canada is already entering claiming the NAFTA duty-preference, a high percentage given the newness of the procedures and the significant proportion of our trade that already entered duty-free.

We also are keeping a watchful eye for any failures to implement the Agreement. We are on the front line in hearing from the business community when a company believes that they are not getting the benefits of the Agreement, both through our daily business counseling and through our formal advisory system (including our 17 Industry Sector Advisory Committees and 3 cross-sectoral advisory groups covering customs, standards and intellectual property rights.) We recognize that the implementation of this Agreement is as important as its negotiation in determining the framework under which NAFTA will develop.

Second, NAFTA has an extensive work program designed to *further liberalize* trade in North America. There are about 25 working groups addressing such practical matters as finding a means for the mutual recognition of professional licenses to developing a trilateral Advisory Committee on Commercial Dispute Resolution. Our biggest effort at the moment is to identify products on which we can agree to accelerate the elimination of tariffs. The U.S. Government alone has received well over 2,000 product petitions from U.S. industry; under the CFTA, tariffs on more than 600 products, worth more than $9 billion, were removed under this process.

Third, several new *institutions* are created by the NAFTA. As mentioned earlier, there are new trilateral institutions on the environment and labor, and new bilateral institutions on border infrastructure and financing. In addition, we have agreed to a North American Trade Secretariat, located in Mexico, that will coordinate administrative matters for the working groups. Locations have been decided for each of these institutions, and draft rules of procedures and draft work plans have been published for most. We are currently dealing with the challenge of finding the right people to head and staff these bodies. There are big challenges for the effective operation of the U.S. national section of the NAFTA Secretariat, which is housed in the Department of Commerce and provides administrative support for dispute settlement. The extent of the demands the U.S. Secretariat will face under a trilateral NAFTA are still unknown, but under the CFTA this unit averaged over 1 million pages of legal papers a year in its "clerk of the court" capacity.

On the financial side, we have taken a major step in increasing our tools to deal with disruptive exchange markets through the creation of the North American Financial Group. This new consultative arrangement will promote orderly exchange markets in North America, facilitating regional trade and investment flows.

Fourth, the U.S. Government has been particularly active in the area of *business outreach*. Through technical seminars, automated systems, and professional staff, the Department of Commerce provides up-to-date information that is critical in enabling the business community to take advantage of the NAFTA.

One of our most effective trade promotion efforts is the well-known "Export Mexico" program, which focuses the efforts of the entire Administration on our fastest-growing market. This program has provided literally thousands of businesses with information regarding how to take advantage of NAFTA. In just the first 4 months of 1994, in partnership with Federal Express, we conducted over 70 seminars across the nation that instructed 17,000 U.S. exporters on the nuts and bolts of NAFTA's customs documentation. Additional seminars, co-sponsored by UPS under our "Big Emerging Markets" initiative, will be haled throughout 1995. "Export Mexico" also provides on-going counselling efforts to U.S. companies to help them identify trade opportunities in Mexico. Business interest is intense: so far in 1994, our Embassy in Mexico has experienced a 50 percent increase in trade promotion events, while our automated information system, "NAFTA Facts", has averaged 30,000 documents a month.

Finally, *maintaining public support* for the NAFTA will be critical, not only for the success of the NAFTA, but to future trade agreements as well. The Department of Commerce is constantly monitoring business response to NAFTA. "Success stories" provide encouragement to other firms to test their wings with Mexico and are distributed via our biweekly "NAFTA News." Congress requires a full report on the economic impact of NAFTA in 1997.

VIII. Implications for the Future

Signing the NAFTA isn't a conclusion — it is a beginning. The framework exists, but the reality is being created. We face four key challenges to NAFTA's success.

A. Challenge #1: Harmonization Issues

Integration means greater and more open competition. NAFTA has dismantled the traditional barriers to trade and investment, but like the proverbial onion, underneath there are more layers to peel away. The absence of trade barriers makes the significance of other policy differences loom much larger.

These harmonization issues — differences in legal systems, regulatory policies, competition policies, tax policies, exchange rate policies, etc. — are the future agenda of global trade talks, but we will confront them first in NAFTA. As deeper integration extends to areas previously considered "domestic," it is in our mutual interests to explore as many avenues as we can for finding common ground on these issues. Some mechanisms are contained within the NAFTA itself — for example, the trilateral Working Group on Trade and Competition and the trilateral Work Groups set up at Canada's request to explore new approaches to subsidy and antidumping issues.

NAFTA has already inspired some progress. Mexico passed a new competition law in 1993 that was widely praised in the United States, and suggests we can learn from each other. John Clark, a top U.S. antitrust enforcement official, noted that in contrast to the United States — where it took 100 years to develop the notion that antitrust law protects competition, not competitors — Mexico's new law explicitly recognizes that economic efficiency should be the touchstone of antitrust enforcement and can immediately begin "protecting the process of competition."

Of course, governments are not the only players here. I am quite impressed with the private sector initiatives to try to close the gap in commercial practices that arises from differences in our legal systems.

One such group is the National Committee on Uniform Transportation Law and Practices, which is working to develop a common approach to how North America compensates for cargo damages and losses. This trilateral, grass-roots effort has among its participants lawyers, freight-forwarders, transporters and shoppers; even government officials have been invited to sit in on the panels.

This effort illustrates the many differences that can plague business "as it is practiced." For example, in the U.S. and Canada, it is assumed the carrier receives merchandise in good condition and is responsible for its safe transit; in Mexico, this is the equal responsibility of the owner of the goods and the carrier. Compensation issues are also treated differently: Mexico applies a formula based on weight that can yield very low recovery rates, while tariffs filed with the ICC by U.S. common carriers determine the limits of their liability. As simple a practice as the Mexican requirement that a plaintiff show the original bill of lading can reduce the ability to sue, since the bill is often retained by the carrier until final payment is made.

To fully capture the benefits of free trade, we need to clear away the underbrush that keeps us from having a truly integrated market.

B. Challenge #2: Managing State/Provincial Relations

Another challenge we have to address in the future is how to incorporate subcentral governments into our integration efforts.

The manner in which states/provinces interact with increasing integration is complex. As mentioned before, effective cross-border integration is often being led by entities below the federal level. For example, the Alberta-Montana agreements on truck safety and licensing, or the work that has been done on the I-5 Pacific Northwest corridor are positive initiatives undertaken by state and provincial authorities.

In other areas, the overlapping jurisdiction between federal and subfederal governments (or the lack of federal jurisdiction) can complicate solutions to integration problems and new market openings in free trade areas. For example, measured commitments under NAFTA's side agreements reflect in part the fact that jurisdiction of many environmental and labor issues rests with the states and provinces in the U.S., Mexico and Canada, not with the federal governments. Similarly, some of the most implacable disputes between the U.S. and Canada involve issues where jurisdictions rest with the Canadian provinces, such as beer and softwood lumber. In other instances, especially along the border, subcentral governments may desire to move toward greater regional integration, but balance this with the desire to keep intact their jurisdictional prerogatives vis-a-vis the federal government.

Finally, there are areas where states/provinces are lagging behind the federal embrace of more open markets and greater integration. How integration is viewed is seen through the lens of how it affects local interests. Potential problem areas are already clear:

— In the services sector, states and provinces are the relevant licensing bodies and can act to prevent professionals from other countries from providing that service. Several states, for example, require applicants to engineering exams to be U.S. citizens, an insurmountable hurdle if you are not one. (Exclusionary impulses aren't limited to international borders; states often fail to offer reciprocity to engineering and medical professionals even when they have passed an identical exam in another state.) These practices can make it difficult to realize free trade in some services.

— Local governments are major economic players in their own right. In procurement, U.S. states spend more than $210 million for goods, services and structures, while the U.S. federal government spends just $80 billion in non-defense expenditures. Expanding NAFTA's coverage of government procurement to state and local governments would require them to overcome the inherent preference to provide advantages to local firms.

— States and provinces are increasingly active in providing incentive packages for companies to invest/remain within their jurisdictions. South Carolina reportedly provided $150 million in incentives for BMW, while Alabama provided close to $300 million for Mercedes. We can expect this competition for mobile factors of production to be even more intense in an integrated North American economy, as the free movement of goods and capital within NAFTA generates new pressures for "one-better-thy-neighbor" policies.

A big problem is that local governments often champion local interests at the expense of consumers and the national welfare, because their politicians are closer to constituents who oppose change in the status quo.

Our challenge, then, is to expand free trade "inward", to bring our local governments on board to the advantages of free trade without alienating them. If we are successful in NAFTA, it will also strengthen our hand in future international negotiations, which are likely to target local services and investment restrictions as they become one of the few protectionist barriers left to defend.

NAFTA provides a mechanism for getting a head start on this process. Through its provisions for consultations with state/provincial and regulatory agencies on areas within their jurisdiction, it provides us with an opportunity to extend liberalization without undermining their authority.

C. Challenge #3: Facilitating Adjustment

NAFTA is critical to North America's ability to compete in a global economy and to create more and better-paying jobs. For this process to work, however, we have to be prepared to accept greater competition and inevitable adjustments.

While the sharpest debate on NAFTA was in the United States, in truth, the short-term burden of structural change for the long-term benefit of enhanced efficiency may be greatest in Mexico and Canada. All economic studies agree that relatively speaking, Mexico and Canada will derive the greatest benefits from integration under NAFTA as they remove higher initial barriers and derive greater potential increases in economies of scale. But Mexico and Canada will have to adjust the most, too.

Maintaining support of NAFTA during this adjustment is a serious political challenge. We will be helped by the fact that NAFTA's provisions are phased in over 15 years for those industries most likely to find difficulty competing in an open environment, providing them time to develop niche strengths and, where necessary, "adjust out." Other factors, however, may add to the difficulty — Mexico's challenge to meet the requirements of free trade while conducting communal land reform and meeting the needs of peasant communities is one that is commonly cited.

It is our joint responsibility to do what we can to facilitate this adjustment within the rules of NAFTA. Fortunately, each of us has taken initial steps.

For example, former President Salinas worked to strengthen Mexico's vocational training program in cooperation with the private sector. [We expect this to continue under the new Zedillo Administration.] In addition, Mexico's Procampo program will provide income supports to help Mexico's large population of small farmers adjust to ejido reform and greater competition under NAFTA. Reductions in the interest rate provided by Mexico's development banks to small businesses will help this innovative, job-creating sector qualify for credit to modernize and take advantage of NAFTA's new opportunities.

For the United States, a key element in U.S. NAFTA legislation was a provision for trade adjustment assistance, which already has certified several thousand U.S. workers for income support and training while they upgrade their skills. President Clinton will introduce legislation next year to replace this NAFTA-specific program with a comprehensive, national "no fault" training program designed to dramatically increase the flexibility and forward-looking skills of the U.S. work force.

Given the limited trade between Canada and Mexico that currently exists, the Government of Canada has focused its resources not on trade adjustment but on a strong export promotion program. Canada has earmarked approximately $23 million over four years to help large and small Canadian firms take advantage of new business opportunities under NAFTA. Targeted sectors include advanced technology, agri-food, environmental technologies, and services. The federal government plans to sponsor approximately 30 trade missions to Mexico, to which it expects the provinces to conduct 30 more. In March 1994, Canada sponsored an international trade expo in Mexico for 425 companies designed to bring Canadian firms together with Mexican counterparts. You can be sure we'll be watching their efforts closely for new ideas.

Such programs are critical to helping our citizens adapt to changed competitive opportunities in an integrated North America.

D. Challenge #4: Sound, Broad Economic Policies

The Clinton economic program in the United States, combined with Mexico's impressive economic reforms and Canada's recent economic recovery, have all combined to fuel investment and growth in our region. Most analysts are forecasting growth this year in the 3-4 percent range in the U.S. and Canada, and are predicting a credible upswing in Mexico's economy despite the difficult political developments this year. This makes North America one of the few bright spots on the immediate international economic horizon, as Europe and Japan continue to struggle for an economic upturn.

In 1993, the US GDP was 87 percent of North American GDP. It stands to reason that what we do — or fail to do — has *enormous* reverberations in Canada and Mexico. It is for this reason that the following policies of the Administration, though centered on the U.S., will also have a positive impact on our neighbors.

President Clinton has:

- — set the stage for very significant declines in the U.S. budget deficit;
- — begun new programs to educate and train the workforce, an essential step in our ability to compete in the world economy;
- — created research and development partnerships between the government and industry in a wide range of "industries of the future";
- — given attention to America's pressing social agenda, including health care, welfare reform and anti-crime legislation.

Taken together, these measures will contribute to economic growth, more competitive industries, and a more productive and secure population — all leading not just to more trade, but to an even stronger political consensus in favor of a more open trading system.

IX. Conclusion

If you watch the trade headlines these days, you would think that the biggest questions facing the U.S. — and the biggest stakes — are in China or Japan or Europe. You would see very little about North America as such. But in my view, what is happening in our backyard is every bit as significant as these other issues.

Maybe North American integration isn't so sexy because it doesn't raise tensions of "geostrategic" importance. But make no mistake about it, the interaction among the United States, Canada, and Mexico is of momentous significance. There is a "geoeconomic" and "geosocial" dimension to what is happening on our continent, and in the post-Cold War era these dimensions count more than ever.

First, we are witnessing a degree of economic integration that is approaching what has been going on in Western Europe — only they started many decades before us. There *is* a North American market, and it is going to continue to develop.

It is interesting to note that we don't quite know what to call this phenomenon. Is it a North American Common Market, with the rules of origin acting in place of a common external tariff? Is it a new kind of new "economic system"? Is it a North American Community with characteristics that go well beyond economic integration? Is it too complex to define at all?

On one level, it is not a bother not to be able to label this North American phenomenon. On another, we need a vision of where we are headed. On the heels of a hard won NAFTA debate, it is perhaps too early to tackle this question. But the question looms, and leaders in both the public and private sectors will need to articulate not just where we are, but where we want to go.

Second, the mix of factors affecting our integration experience makes North America unique. It includes both highly industrial nations *and* a developing country. By contrast, the European Union is much more homogeneous. Also, North American integration is propelled by business and economic forces, and by an underlying need to open our economies to better compete in the world. By contrast, the impetus for European integration has had a much greater political dimension. North American integration, moreover, is being driven by both business pressures and governmental actions — both from the bottom and from the top — and also by a wealth of subfederal entities like cities and port authorities. In my view, this is a microcosm of the multi-faceted but inexorable way the world economy will be coming together in the years ahead.

Third, the success of NAFTA will have significant impact on America's future trade policy. NAFTA is a state-of-the-art trade agreement, encompassing as it does a very broad range of issues from services to intellectual property rights, and agreements on the environment and labor standards. How we handle the implementation of NAFTA, and our experience with the agreement, will have a great bearing on how we approach future trade negotiations on a regional and global level. In this respect, the stakes in succeeding are very high.

Fourth, there is a very high premium on effective follow up to NAFTA. We must not succumb to the temptation to think that the conclusion of the treaty ensures that NAFTA will work. There is much work to do. All three governments need to continually review the overall picture to ensure that the many aspects of follow up are given a high priority. There must be a constant temperature taking of the overall trends and problems in North America.

In this regard, we need to be careful about backsliding in a range of areas. Trade liberalization may have gotten a boost with the NAFTA, but history shows there is often a second phase in which selected efforts are made to arrest inevitable change. President Clinton's admonition "compete, not retreat" must be our watchword, along with a strong effort to cushion change for men, women and families who need help. But we must move forward.

The United States is committed to working with both the Cretien Administration in Canada and the newly-elected Zedillo Administration in Mexico to foster needed change in the most humane way. We are committed to continuous expansion of trade in North America, to the development of effective institutions to facilitate that trade, and to deal with the broader economic and social issues. We are deeply committed to making NAFTA work for all of us.

The continuing integration of the North American market will serve all three countries exceedingly well. Of course there will be many bumps in the road, but the trends are positive and I am confident that we will surmount the challenges — economic and social — that we will face. Many questions have been raised by Asian governments and business executives about the possibilities of joining NAFTA. This, of course, was nothing compared to the interest in Latin America. The point is that much of the world is sensing that we are building a dynamic and prosperous market like no other.

A North American consciousness is building among our three countries. There are no headlines describing it, and that is probably a good thing. Let us build our market quietly, and steadily, using practical building blocks, resolving disputes amicably, and summoning the political will to deal with problems as they arise in a North American context. Let's look for ways that all three countries can benefit. Let's show that zero-sum solutions don't make sense for North America. Let's show that we in North America understand the true nature of the requirements for deep seated cooperation in this rapidly changing global economy.

LIST OF TABLES AND APPENDICES

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TABLE 1: Selected U.S.-Canada Treaties and Agreements

AGREEMENT: U.S.-Canada Boundary Agreement
YEAR: 1908
PURPOSE: Commitment between Canada and the United States to survey and maintain and manage land boundary issues.

AGREEMENT: U.S.-Canada Boundary Waters Treaty
YEAR: 1909
PURPOSE: Bilateral cooperation in managing boundary waters; established the principle that neither country should exploit the waters in a manner that would damage the interest of the other. Created International Joint Commission (IJC) charged with overseeing water management, later, broader areas of transborder environmental protection/conservation.

AGREEMENT: Migratory Birds Convention
YEAR: 1916
PURPOSE: Bilateral convention for the protection of migratory birds in the United States and Canada.

AGREEMENT: Ogdensburg Declaration
YEAR: 1940
AGREEMENT: Hyde Park Agreement
YEAR: 1941
PURPOSE: Foundation declaration and agreement arising from beginning of WWII in which the United States and Canada agreed, as a general principle, to coordinate and rationalize the defense industries of both countries. Founded the Permanent Joint Board on Defense. Memorandums of Understanding such as Defense Production Sharing Agreements and the Defense Development Sharing Agreement (1963) followed. Provided for standardization/interoperability of defense equipment, data exchange, contract administration, committee creation, and other mechanisms to facilitate coordination of Canada-U.S. defense efforts.

AGREEMENT: St. Lawrence Seaway Agreement
YEAR: 1952
PURPOSE: Agreement establishing the St. Lawrence seaway project for the construction of certain navigation facilities.

AGREEMENT: Convention on Great Lake Fisheries
YEAR: 1954
PURPOSE: Established the Great Lakes Fishery Commission which coordinates the U.S.-Canada Great Lakes fishery management plan (1978). Provided pooled lakewide/basinwide responsibilities to ensure effective management of the Great Lakes' fishery resources.

AGREEMENT: Columbia River Treaty
YEAR: 1964
PURPOSE: Provides for cooperative development of the water resources of the Columbia River Basin.
AGREEMENT: Automotive Products Agreement (Autopact)
YEAR: 1965
PURPOSE: Provides for duty-free treatment of finished vehicles and parts between U.S. and Canada.

AGREEMENT: U.S.-Canada Tax Treaty
YEAR: 1984
PURPOSE: Establishes bilateral understanding on treatment of income and capital earned in each other's respective territory. Presently under renegotiation.

AGREEMENT: Memorandum of Understanding on the Exchange of Import Data
YEAR: 1987
PURPOSE: Established mechanism allowing each country to rely on the other's import data for it's export data.

AGREEMENT: U.S.-Canada Free Trade Agreement
YEAR: 1989
PURPOSE: Established free trade area between United States and Canada providing for the elimination of tariff and non-tariff barriers to bilateral trade.

TABLE 2:
Selected U.S./Canada State/Provincial Arrangements/Agreements

AGREEMENT: Montana-Western Canadian Provinces Boundary Advisory Committee
YEAR: 1983
PURPOSE: Composed of both legislators and executive branch participants; discuss wide range of issues common to the border region.

AGREEMENT: National Association of State Departments of Agriculture/Canadian Provincial Agriculture Secretaries
YEAR: 1984
PURPOSE: Coordinates cross-border issues related to Federal/state/provincial agricultural trade, commodities, standards, and regulations.

AGREEMENT: Great Lakes Charter
YEAR: 1985
PURPOSE: Cooperation agreement between Quebec, Ontario, and 8 U.S. Great Lake states.

AGREEMENT: Agreement of Energy Cooperation between Quebec and New York
YEAR: 1986
PURPOSE: Agreement to cooperate on energy issues of importance between Quebec and New York.

AGREEMENT: Minnesota-Manitoba Agreement on Economic Cooperation and Trade Opportunities
YEAR: 1988
PURPOSE: Provides for improved economic cooperation such that trade and other beneficial economic contacts maximize free trade area opportunities.

AGREEMENT: Memorandum of Understanding on Environmental Cooperation on the Management of Lake Champlain (Quebec/New York/Vermont)
YEAR: 1988
PURPOSE: Enhances and establishes a process for regular exchange of information and systematic cooperation in research and data gathering on subjects affecting Lake Champlain.

AGREEMENT: Pacific Northwest Economic Region (PNWER)
YEAR: 1989
PURPOSE: Formed by legislators from Alaska, Alberta, British Columbia, Idaho, Montana, Oregon and Washington; serves as a steering committee to develop/implement strategies for regional cooperation.

AGREEMENT: Economic Cooperation Arrangement on Trade, Investment and Tourism Between British Columbia and Alaska
YEAR: 1990
PURPOSE: Establishes venue for increased exchange of information and promotion of trade and economic cooperation.

AGREEMENT: Economic Cooperation Arrangement between British Columbia and California
YEAR: 1990
PURPOSE: Establishes venue for exchange of opinion and information on trade, tourism, investment and other related opportunities.

AGREEMENT: Agreement on Cooperation Between Quebec and New York
YEAR: 1993
PURPOSE: Incorporates and enhances existing individual agreements in energy, environment, public safety, and economic development.

TABLE 3: Intra-North American Investment: 1992 and 1989

BILLIONS OF DOLLARS

	Foreign Direct Investment		*Portfolio Investment*	
	1992	1989	1992	1989
U.S. Investment in Canada	$68.4	$63.9	$79.6	$74.7
U.S. Investment in Mexico	$13.3	$8.3	$22.0[1]	$15.0[3]
Canadian Investment in U.S.	$39.0	$30.4	$71.3	$50.2
Canadian Investment in Mexico	$0.4	$0.4	$0.2[1]	$0.1[1]
Mexican Investment in U.S.	$1.2	$0.4	$2.4[1]	$1.8[1]
Mexican Investment in Canada	$0.1	—	—[1]	—[1]
Total Intra-North American Investment	$122.4	$103.4	$175.5[2]	$141.8[2]
% Increase in Total Intra-North American Investment 1992-1989	18%		24%	

Sources: U.S. Bureau of Economic Analysis (BEA); Industry Canada; Statistics Canada

[1]Unpublished estimate.
[2]Portfolio totals should be viewed as estimates given their incorporation of unpublished data.
[3]1991 estimate substituted for unavailable 1989 data.
(—) Negligible

TABLE 4: Intra-North American Trade for 1992

MILLIONS OF DOLLARS

Top 5 U.S. Exports to Canada

Motor Vehicles and Parts	$17,107
Industrial Machinery and Computers	14,944
Electric and Electronic Equipment	10,988
Chemical Products	7,065
Fabricated Metal Products	4,771

Top 5 Canadian Exports to U.S.

Motor Vehicles and Parts	$27,510
Crude Petroleum	8,135
Paper Products	7,862
Primary Metal Products	7,188
Industrial Machinery & Computers	5,779

Top 5 U.S. Exports to Mexico

Electric and Electronic Equipment	$7,144
Industrial Machinery and Computers	5,690
Motor Vehicles and Parts	3,897
Chemical Products	2,943
Primary Metal Industries	2,924

Top 5 Mexican Exports to U.S.

Electric and Electronic Equipment	$9,663
Motor Vehicles and Parts	4,998
Crude Petroleum	4,424
Apparel	1,962
Industrial Machinery and Computers	1,773

Top 5 Canadian Exports to Mexico

Motor Vehicles and Parts	$121
Cereals	97
Electric and Electronic Equipment	60
Iron & Steel	52
Paper Products	44

Top 5 Mexican Exports to Canada

Motor Vehicles and Parts	$952
Electric & Electronic Equipment	415
Machines & Mechanical Appliances	338
Mineral Fuels & Oils	156
Furniture	92

TABLE 5: Intra-Firm Trade: Merchandise Trade by Related Parties, 1992

PERCENT

	With North America	*With Rest of World*
Total U.S. Trade	47.0%	35.5%
U.S. Exports	43.2	26.3
U.S. Imports	50.5	43.2
	With Canada	*With Mexico*
U.S. Exports	45.3%	38.7%
U.S. Imports	46.0	63.6
	With Other Industrial	*With Other Developing*
U.S. Exports	34.7%	17.8%
U.S. Imports	45.9[1]	27.9

Source: "U.S. Merchandise Trade: Imports & Exports by Related Parties; 1992," U.S. Department of Commerce, April 6, 1994. (CB-94-60)

Definitions: North America includes Canada and Mexico. Other Industrial countries incudes the EC and Japan for exports, and the EC for imports (see footnote 1). Other Developing countries includes OPEC, Taiwan, Korea, and "Other," which excludes Eastern Europe, the former USSR, and China.

[1]Seventy-five percent of U.S. imports from Japan are from a related party, a much higher percentage than for any other country; in contrast, about 46 percent of U.S. imports from both the EC and Canada are from a related party. Japan is not included in the import figure to avoid giving an erroneous impression of what is typical for U.S. imports from industrial countries.

TABLE 6: U.S.-Mexico Border Infrastructure Projects in Development

Project Location	*Sector/Project Type*	*Value (M$USD)*
Tijuana, Mexico	Waste Water Treatment Plant	16.9
Cd. Juarez, Mexico	Waste Water Treatment Plant	29.8
Matamoros, Mexico	Waste Water Treatment Plant	12.0
Mexicali, Mexico	Waste Water Treatment Plant	7.2
S.L. Rio Colorado	Waste Water Treatment Plant	5.6
Ciudad Acuna, Mexico	Waste Water Treatment Plant	3.5
Nuevo Laredo, Mexico	Waste Water Treatment Plant	9.4
Reynosa, Mexico	Waste Water Treatment Plant	4.5
Nogales, Mexico	Solid Waste Processing Facility	3.2
Tijuana, Mexico	Airport Expansion/Modernization	189.4
N. Baja California	Power Generation Plant (IPP)	400.0
Tamaulipas, Mexico	Power Generation Plant (IPP)	1,800.0
Reynosa, Mexico	Border Crossing Access Road	8.0
Reynosa-Matamoros	Tollroad	188.0
S.L. Rio Colorado	Tollroad from Sonoyta	190.0
Mexicali, Mexico	Tollroad to Tecate	297.0
Nogales, Mexico	Highway Beltway	23.8
Nuevo Laredo, Mexico	Highway Beltway	17.4
Cd. Juarez, Mexico	Rail Ringway Project	43.8
Tijuana, Mexico	Modernization of Border Crossing	61.0

ANNEX 1: North American Integration

MERGERS, ACQUISITIONS, EQUITY INFUSIONS, JOINT VENTURES

SECTOR: Food

INVESTOR: Abastos y Promociones (Mex)

TYPE OF INVESTMENT: Plans to open McAllen Produce Terminal Market (US).

COMMENTS: Facilitates exportation and importation of produce for US & Mexican growers. ($20 million investment)

DATE: Summer '94

INVESTOR: Tyson (US)

TYPE OF INVESTMENT: Acquired majority interest and managerial control of Trasgo (Mex), a poultry producer and processor.

COMMENTS: Tyson has been a minority partner since '88. Allows them to increase presence in Mexican market.

DATE: April '94

INVESTOR: Sara Lee (US)

TYPE OF INVESTMENT: JV with AXA (Mex) to invest in its subsidiary, AXA Alimentos (Mex).

COMMENTS: Expands marketing expertise in processed meat industry.

DATE: March '94

INVESTOR: Pillsbury (US subsidiary of UK company)

TYPE OF INVESTMENT: 49% stake in JV with Pacific Star de Occidente (Mex), formed new company Pacific Star (Mex).

COMMENTS: Expands distribution and sales capacity in Mexico.

DATE: September '93

INVESTOR: Oscar Meyer (US)

TYPE OF INVESTMENT: Distribution agreement with Sigma Alimentos (Mex).

COMMENTS: Expands marketing & distribution in Mexico. First phase of strategic alliance.

DATE: April '93

INVESTOR: ConAgra (US)

TYPE OF INVESTMENT: JV with Maple Leaf Foods (Can) to create two flour milling companies in US & Canada.

COMMENTS: Improves efficiency for both and moves ConAgra Flour Milling into new markets and new lines of business in Canada.

DATE: May '92

Investor: Cargill Inc. (US)

Type of Investment: Addition of slaughterhouse in Alberta, Canada to expand capacity.

Comments: Capitalize on Alberta's location as a large cattle producing region and its proximity to western U.S. markets.

Date: 1989

SECTOR: Telecommunications

Investor: MCI (US)

Type of Investment: JV with Grupo Bannaci (Mex).

Comments: Provide competitive long distance service in Mexico. ($450 million investment)

Date: January '94

Investor: GTE (US)

Type of Investment: JV with Telmex (Mex), combined with already existing partnership with Skytel Communication Corp. (Can).

Comments: Allows airline passengers to place phone calls from the air to business centers throughout North America.

Date: December '93

Investor: AT&T (US)

Type of Investment: AT&T receives a 20% equity investment in Unitel (Can) long-distance telephone company.

Comments: Establishes feeder network that allows Unitel and AT&T to offer transborder services to multinational customers. Unitel receives access to AT&T's intelligent network software. (Investment valued at $150 million — Canadian)

Date: February '93

SECTOR: Beer

Investor: Anheuser Busch (US)

Type of Investment: Acquired equity stake in Grupo Modelo (Mex).

Comments: Allows for a 17.7% equity stake in Mexican brewer ($477 million). Sole Busch importer and distributor in Mexico.

Date: May '93

Investor: Miller (US)

Type of Investment: Strategic alliance with The Molson Companies Limited (Can) and Foster's Brewing Group.

Comments: Miller acquired US import operations of Molson Breweries and the US marketing and distribution rights for Molson and Foster's brands in the US. Miller also received a 20% equity share in Molson Brewery.

Date: April '93

SECTOR: Transportation

Investor: Canadian National Railways (Can), KLLM (US)

Type of Investment: Alliance which allows the two companies to move fresh produce from California, the Gulf Coast and Mexico to Canada. The service will carry processed food from Canada on the return journey.

Comments: Allows CN to take advantage of opportunity to increase intermodal traffic between US, Canada and Mexico. Positions KLLM to take advantage of return traffic.

Date: November '93

SECTOR: Steel

Investor: Ipsco Steel (Can)

Type of Investment: Planned construction of a steel mini-mill in the US.

Comments: Location is to be in Iowa, subject to approval by Iowa government. Production projected in 1996. Should help in reducing inventory and carrying costs. ($360 million investment)

Date: September '93

SECTOR: Financial Services

Investor: Western Union (US)

Type of Investment: JV with Elektra (Mex).

Comments: Provides money transfer service from U.S. to Mexico.

Date: December '93

Investor: Standard & Poor's Ratings Group (US)

Type of Investment: Acquired all outstanding shares of Calificadora de Valores (CAVAL) (Mex), Mexico's largest rating agency. The rating agency will be called S&P-CAVAL

Comments: Allows S&P to better meet the needs of the Mexican capital market.

Date: September '93

Investor: Bank of Nova Scotia (Can)

Type of Investment: Acquired interest in Grupo Financiero Inverlat (Mex).

Comments: 5% percent interest in Mexico's fourth largest financial group. A technical services agreement was also reached. Will help better serve needs of customers doing business in Mexico ($75 million investment).

Date: 1993

Investor: Caisses Dejardins (Can)

Type of Investment: Established branch operations in Allendale, Florida.

Comments: Enables them to better serve growing Canadian community and business clients in Florida.

Date: 1992

Investor: Grupo Finsa (Mex), Texas Pacific Group (US), Richard Blum & Associates (US), and Sturn & Associates (US).

Type of Investment: All are owners of Banco Allianza (Mex). Will have operations in Matamoros, Mexico City, Monterrey, and Victoria.

Comments: Enhance the ability to serve needs of US businesses and small to medium sized Mexican companies.

Date: April '94

SECTOR: Insurance

Investor: Alexander & Alexander (US)

Type of Investment: Acquired stake in Asesores Kennedy Agente de Seguros (Mex).

Comments: 80% interest in the insurance broker, better positions A&A to take advantage of growing Mexican insurance market.

Date: January '94

Investor: Liberty Mutual (US)

Type of Investment: Opened office in Mexico City, Servicios Liberty.

Comments: Provide occupational health and safety services and products to companies in Mexico.

Date: January '94

Investor: Johnson & Higgins (US)

Type of Investment: Acquired stake in Brockman y Schuh (Mex).

Comments: 25% of the Mexican insurance firm. Expands service capabilities in Mexico.

Date: November '93

Investor: New York Life (US)

Type of Investment: Acquired stake in Geo, Compania de Seguros (Mex).

Comments: Acquisition of 30% interest in the life insurance firm. Will offer life insurance services in Mexico.

Date: October '93.

Investor: Chubb (US)

Type of Investment: Acquired interest in Seguros Equitativa, and its affiliate, Central de Fianzas (Mex).

Comments: 30% interest in both the insurance, and the surety and bonding companies.

Date: Summer '92

Investor: Metropolitan Life Insurance Company (US), Banco Santandar (Spain), Various Mexican investors.

Type of Investment: JV with Banco Santandar (Spain to form Seguros Genesis.

Comments: 49% of JV owned by MetLife and Banco Santandar, with rest held by other Mexican investors. Is MetLife's first venture into Latin American, and is an opportunity to participate in a market where there is large growth potential. Seguros Genesis will sell life insurance and pension products.

Date: August '92

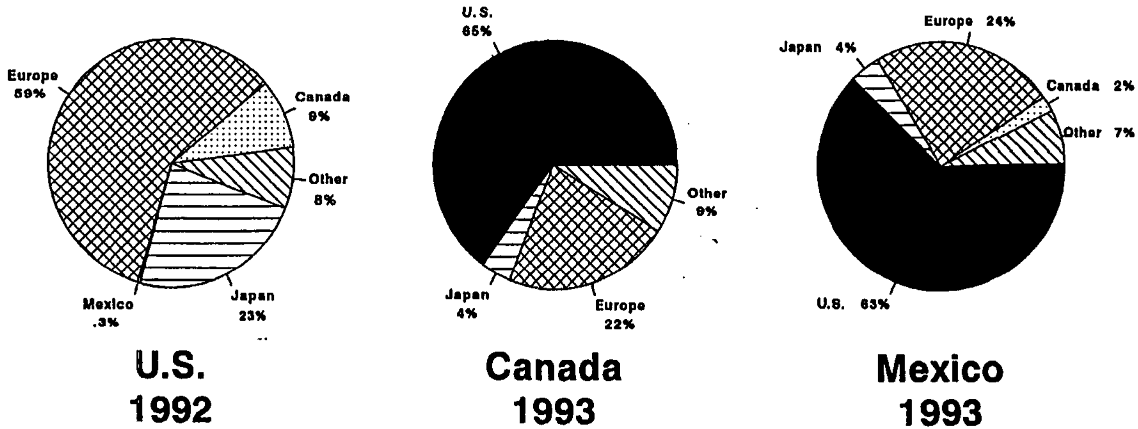
The Department of Commerce would like to thank Dr. Fernando Robles of The George Washington University for his assistance in compiling this information.

FIGURE 1

FOREIGN DIRECT INVESTMENT IN NORTH AMERICA

BY COUNTRY OF ORIGIN

The U.S. is by far the dominant foreign investor in Canada and Mexico, but Canada and Mexico account for a small proportion of FDI in the United States.



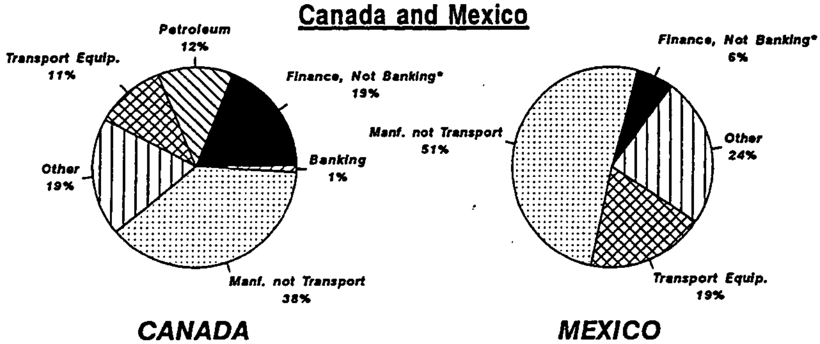
Source: U.S. Bureau of Census

FIGURE 2

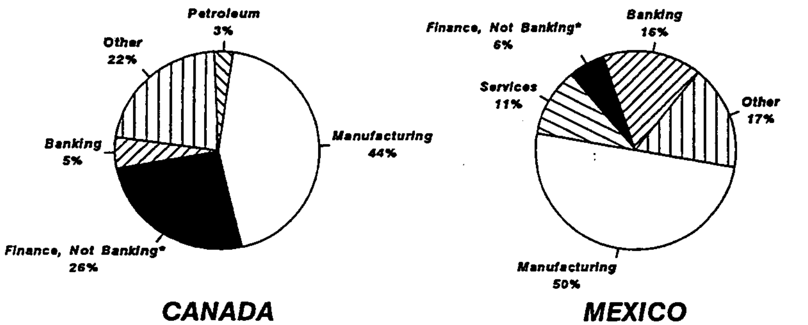
U.S. FOREIGN DIRECT INVESTMENT

BY SECTORS, 1992

U.S. Investment in Canada and Mexico



Canadian and Mexican Investment in the U.S.



*Includes Real Estate and Insurance

FIGURE 3

PERCENTAGE GROWTH IN U.S., CANADIAN, MEXICAN EXPORTS TO NORTH AMERICA AND REST OF WORLD

INTRA-NORTH AMERICAN EXPORTS GROWING MORE THAN TWICE AS FAST THAN TO REST OF WORLD

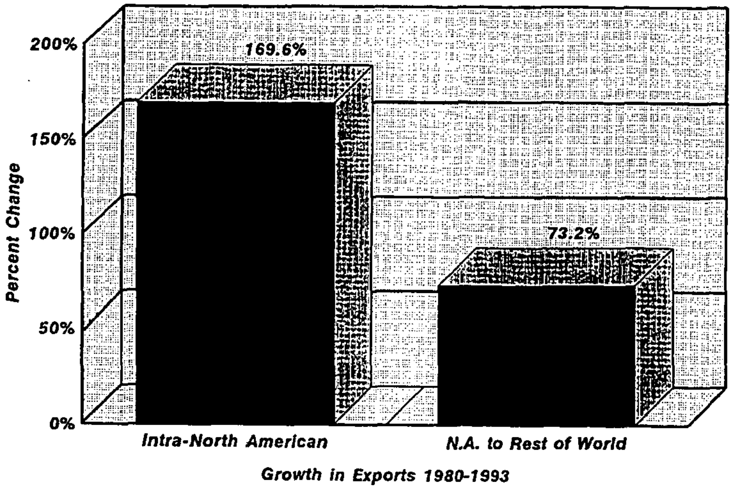


FIGURE 4

INTRA-NORTH AMERICAN EXPORTS AS PERCENT OF TOTAL NORTH AMERICAN EXPORTS: 1980, 1993

INTRA-NORTH AMERICAN EXPORTS SOON WILL ACCOUNT FOR HALF OF NORTH AMERICAN EXPORTS TO THE WORLD

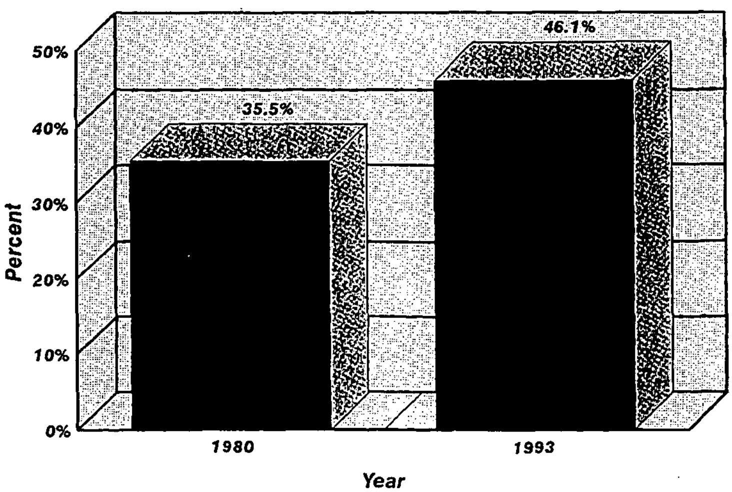
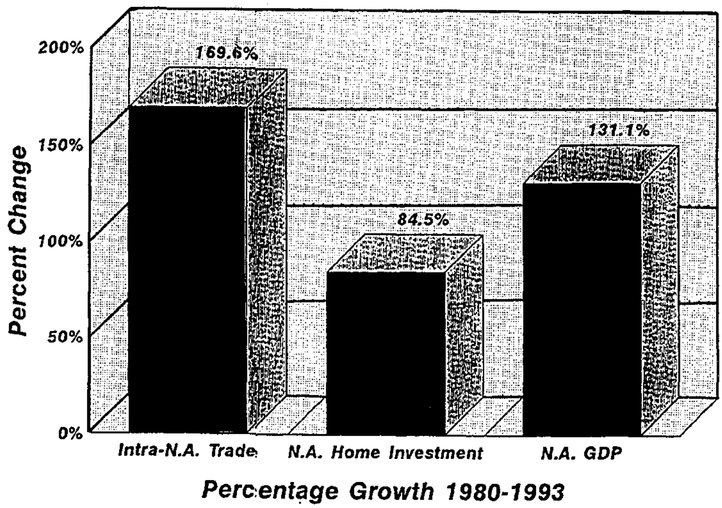


FIGURE 5

GROWTH IN INTRA-AMERICAN TRADE, INVESTMENT AND INCOME

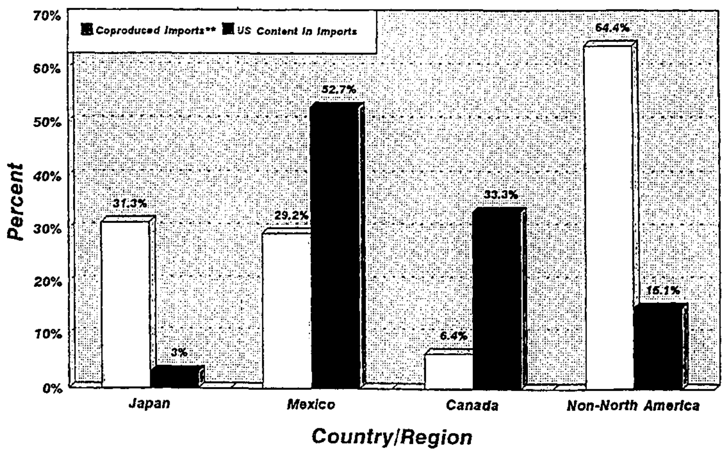


CANADIAN AND MEXICAN DATA IS 1992, EXCEPT MEXICAN INVESTMENT
Source: U.S. Bureau of the Census

FIGURE 6

IMPORTS UNDER SECTION 9802 (CO-PRODUCTION) AND PERCENTAGE U.S. COMPONENTS, 1992

U.S. COMPONENTS IN PRODUCTION-SHARING IMPORTS FROM MEXICO/CANADA MUCH HIGHER THAN TO REST OF WORLD



**Left column represents percent of Imports under Section 9802
Source: U.S. Bureau of the Census